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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1937

No. 342

C. C. McCOLLUM, TRUSTEE IN BANKRUPTCY OF LOOKOUT PLANING MILLS,

Petitioner,

vs.

HAMILTON NATIONAL BANK OF CHATTANOOGA.

PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF TENNESSEE AND BRIEF IN SUPPORT THEREOF.

JOSEPH W. THOMPSON,
Counsel for Petitioner.

JOSEPH B. ROBERTS,
FRED B. FRAZIER,
FRED B. BALLARD,
Of Counsel.

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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1937

No. 342

C. C. McCOLLUM, TRUSTEE IN BANKRUPTCY OF LOOKOUT PLANING MILLS,

Petitioner,

vs.

HAMILTON NATIONAL BANK OF CHATTANOOGA.

PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF TENNESSEE.

To the Honorable Charles Evans Hughes, Chief Justice of the United States, and the Associate Justices of the Supreme Court of the United States:

Your petitioner respectfully shows:

I.

Summary Statement of the Matter Involved.

This is a suit in equity, in the nature of an action of debt, brought in the Chancery Court at Chattanooga, Tennessee, by petitioner herein, trustee in bankruptcy of the Lookout Planing Mills, against the Hamilton National Bank of Chat-

tanooga, in which petitioner seeks to recover the penalty provided by the National Banking Act, U. S. Revised Statutes, Sections 5197, 5198, 12 U. S. C. A., Sections 85, 86, for the charging and taking of usurious or illegal interest (R. 1, *et seq.*).

Respondent filed an answer and cross-bill, alleging the bankrupt was indebted to it in the sum of $25,493.70, and praying that it be allowed to set off the amount thereof against any recovery complainant might have against it (R. 10).

Petitioner answered the cross-bill, alleging that his right of action was conferred by U. S. Revised Statutes, Sections 5197, 5198; that the remedy conferred thereby was exclusive, and that any recovery he might obtain against respondent was not subject to the payment of any obligation of the bankrupt to it (R. 12).

The Chancellor (R. 59-61); the Court of Appeals (R. 64-74) and the Supreme Court (R. 79-84) concurred in finding that the defendant Hamilton National Bank had, within the two-year period prior to the filing of the bill, knowingly charged to and received from the Lookout Planing Mills interest in excess of six per cent to an amount aggregating $5,235.55; and those Courts entered decrees in favor of petitioner for double that sum, or $10,471.10 (Chancellor, R. 61, Court of Appeals, R. 84).

The Chancellor was of opinion (R. 60, 61) that *after judgment* petitioner's claim was subject to set off, and accordingly ordered that the decree awarded petitioner be applied as a set off against or credit upon the indebtedness of the bankrupt to the defendant (R. 61-64).

Petitioner and respondent appealed to the State Court of Appeals (R. 63, 64). That court was of opinion that it would be inequitable not to allow defendant's claim of set off. The Court of Appeals was further of opinion, however, that the right of solicitors for petitioner to a lien for their

fees attached to the judgment and related back to the beginning of the suit, and was thus prior to the equitable right of the defendant to set off, which, the court said "is a floating equity until action by a Court is invoked" (R. 64, 70-74). The Court of Appeals accordingly modified the decree of the Chancellor so as to provide for a lien upon the decree in favor of solicitors for petitioner, and as so modified affirmed the same (R. 74).

Petitions for certiorari were filed by petitioner and respondent, both of which were granted by the Supreme Court (R. 79). That Court was of opinion that the penalty for which suit was brought could only be recovered in an independent action of debt, as directed by the Federal statute, but was further of opinion:

> "*Having obtained a decree for the penalty,* there is no provision in the Banking or Bankruptcy Acts restricting or prohibiting the offsetting of the same with any just debt owing to it by the bankrupt, and, as previously stated, this is expressly authorized by our statute." (Italics ours.) (R. 79, 82.)

The Supreme Court held that such offset is permissible under Section 68 (a) of the Bankruptcy Act, and expressly authorized by Section 8769 of the Tennessee Code, and the petitioner "will be required to do equity by having his claim credited on the larger one owing to the defendant" by the bankrupt (R. 81, 82; R. 84, 85). It was further held by the State Supreme Court that solicitors for petitioner did not have a lien on the decree for counsel fees. The decree of the Court of Appeals was modified accordingly, and as so modified was affirmed by the Supreme Court (R. 79-84; R. 84).

Your petitioner presents to this Court and files herewith a duly certified transcript of the entire record in the case as the same appears in the Supreme Court of the State of Tennessee.

The principal questions involved on said appeal may be summarized as follows:

(1) Did petitioner, as trustee in bankruptcy of the Lookout Planing Mills, have the right to recover the penalty provided by U. S. Revised Statutes, Section 5198, 12 U. S. C. A., Section 86, in "a suit brought specially and exclusively for that purpose," without the presentation or consideration by the Court of any counterclaim of the respondent based upon the balance owing it by the bankrupt?

(2) The respondent bank held an unsecured claim against the estate of the bankrupt, duly proved, and the trustee of the bankrupt had a claim for the penalty aforesaid, upon which he was awarded a decree against respondent bank for $10,471.10. Were these such "mutual debts or mutual credits" as could be set off one against the other under Section 68 of the Bankruptcy Act (11 U. S. C. A., Section 108)?

(3) Did the Court have the right under Section 8767 of the Code of Tennessee or under general principles of equity jurisprudence to direct the application of the indebtedness of the bankrupt to respondent as a set off against the decree in favor of petitioner?

These questions were decided by said Supreme Court and materially affected the final determination of said cause.

II.

Reasons Relied Upon for Allowance of the Writ.

(1) *Conflict With Applicable Decisions of This Court.*

This Court has uniformly held, in suits brought by national banks against borrowers, that the penalties and forfeitures, and the mode and remedy of enforcing them as prescribed by the Federal statute, are exclusive, and that the remedies

provided by the common law or statutes of the States to prevent collection of usurious interest, or to recover back usurious interest paid, have no application to usurious transactions by national banks.

Other courts have held that these decisions apply where the debtor brings a suit "specially and exclusively for the purpose" of recovering the penalty in question, and that the national bank when so sued cannot apply the balance owing to it by the borrower as a set off against or payment of the judgment for the penalty.

It is believed that to deny the right of set off of usurious payments to the borrower when sued by a national bank, and to grant the bank such right when sued by the borrower, would constitute a violation of the Fourteenth Amendment to the Constitution of the United States.

A final determination by this Court of last resort of the question here presented is a matter of very general interest and importance.

(2) *Important Question of Bankruptcy Law.*

Petitioner is seeking recovery of an asset of the bankrupt estate, and whether respondent is entitled to apply the debt of the bankrupt to it as a payment of the decree in favor of petitioner for the penalty is a question which should be finally determined by this Court of last resort, in order that the Bankruptcy Act may be uniformly applied in all the States.

(3) *Important Question of General Law.*

It is of importance both to borrowers and to national banks that this Court reaffirm and apply to the facts of this case the doctrine that where a cause of action arises exclusively under the laws of the United States the right to recover cannot be influenced by local law or usage as to set off or counterclaim.

(4) *Error in Decree of State Court.*

Upon both reason and authority the decree of the State Supreme Court is erroneous, and if allowed to stand will amount to a practical discharge of the bank from its liability of the usury statute, and encourage practices of this character. There will be no punishment of the violator of the statute, and no recompense to the estate of the borrower.

Petitioner annexes hereto his brief in support of this petition, in which he cites and relies upon applicable decisions of this Court and of other courts, under which he verily believes he is entitled to the relief here sought.

WHEREFORE your petitioner respectfully prays that writ of certiorari be granted to review the decree of the Supreme Court of Tennessee, entered May 24, 1937, in the case of C. C. McCollum, Trustee, *v.* Hamilton National Bank of Chattanooga, and that said decree may be reversed by this Honorable Court in so far as it provides that the amount of the indebtedness of the bankrupt to defendant shall be applied as a set off against the decree in favor of petitioner; and that your petitioner may have such other and further relief in the premises as this Honorable Court may deem meet and just.

And your petitioner will ever pray.

C. C. MCCOLLUM (Correct: C. *H.* McCollum), Trustee in Bankruptcy of Lookout Planing Mills,

By J. W. THOMPSON,

Counsel for Petitioner.

JOSEPH B. ROBERTS,
FRED B. FRAZIER,
FRED B. BALLARD,

Of Counsel.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1937

No. 342

C. C. McCOLLUM, Trustee in Bankruptcy of Lookout Planing Mills,

Petitioner,

vs.

HAMILTON NATIONAL BANK OF CHATTANOOGA.

BRIEF IN SUPPORT OF PETITION FOR CERTIORARI.

I.

Opinions in the Courts Below.

The opinion of the Supreme Court of Tennessee (R. 79-84) was rendered May 24, 1937. It is not now reported.

The opinion of the Court of Appeals of Tennessee (R. 64-74) was rendered August 1, 1936, and the opinion of the Chancellor (R. 59-61) was rendered March 6, 1936.

II.

Jurisdiction.

The statutory provision which is believed to sustain the jurisdiction of this Court is Section 237 (b) of the Judicial Code as amended (28 U. S. C. A., Section 344-b), the pertinent portion of which provides:

> "It shall be competent for the Supreme Court, by certiorari, to require that there be certified to it for re-

view and determination, with the same power and authority and with like effect as if brought up by writ of error, any cause * * * where any title, right, privilege, or immunity is specially set up or claimed by either party under the Constitution, or any treaty or statute of * * * the United States."

III.

Statement of the Case.

A full statement of the case has been given in Section I of the foregoing petition (pp. 1-5), which is hereto attached and made a part of this brief.

IV.

Specification of Errors.

(1) The State Supreme Court erred in holding and decreeing that the decrees of the Chancellor and the Court of Appeals be affirmed, in so far as such decrees directed that the indebtedness of the bankrupt to respondent be applied as a set off against or payment of the decree awarded petitioner in the sum of $10,471.10 as a penalty for the charging and taking of usurious or illegal interest (R. 79-84, 84-85).

(2) The State Supreme Court erred in holding that respondent had the right, under Section 68 (a) of the bankruptcy act, to set off the indebtedness of the bankrupt to it against the recovery decreed petitioner in this cause (R. 81).

(3) The State Supreme Court erred in holding that the respondent had the right, under Section 8769 of the Code of Tennessee, and under general principles of equity jurisprudence, to set off the indebtedness of the bankrupt to it against the recovery decreed petitioner in this cause (R. 82).

V.

Summary of Argument.

(1) *Conflict with Applicable Decisions of This Court.*

It is settled by the decisions of this Court that the penalties and forfeitures provided by the Federal statute and the mode and remedy of enforcing them are exclusive of those provided by the State statutes on the subject.

Barnet v. *Muncie National Bank* (1879), 98 U. S. 555, 25 L. Ed. 212;

Haseltine v. *Central National Bank* (1901), 183 U. S. 132, 46 L. Ed. 118.

The several States have with practicable unanimity recognized and followed this rule. The cases are collected in 101 A. L. R. 752, 753.

The remedy of setting off the usurious interest paid against the principal of the obligation in an action thereon by the bank, allowed by the State statute as to usury or set off, or under general equitable principles, has no application to usurious interest paid to a national bank.

Barnet v. *Muncie National Bank* (1879), 98 U. S. 555, 25 L. Ed. 212;

Haseltine v. *National Bank,* 183 U. S. 132, 46 L. Ed. 118;

Planters National Bank v. *Wysong,* 177 N. C. 380, certiorari denied, 250 U. S. 665, 63 L. Ed. 1196.

Other courts have held that the rule works both ways, and that these decisions are applicable where the debtor brings a suit "specially and exclusively for the purpose" of recovering the penalty in question, and that the national bank charging and taking the usurious or illegal interest cannot

apply the balance owing on account of principal as a set off against or payment of the penalty.

Morehouse v. *McRae,* 30 Hun. 628 (reversed on ground of accord and satisfaction, 98 N. Y. 502);
Lebanan National Bank v. *Karmany,* 98 Pa. 65;
Meredith v. *National Bank,* 127 Tenn. 90.

To deny the debtor the right to set off the penalty when sued by the bank, and to allow set off to the bank when sued for the penalty, would be a denial of the equal protection of the laws, in violation of the Fourteenth Amendment to the Constitution of the United States.

Tinsley v. *Anderson,* 171 U. S. 101, 43 L. Ed. 91;
Scott v. *McNeal,* 154 U. S. 34, 38 L. Ed. 896.

The following decisions of this Court are believed to sustain jurisdiction of this Court upon petition for certiorari:

Talbot v. *Sioux City National Bank,* 185 U. S. 182, 46 L. Ed 862;
U. S. v. *Bank of New York,* 296 U. S. 463.

(2) *Right of Respondent to Set Off Under Section* 68 (a) *of Bankruptcy Act.*

As the suit is brought by petitioner as trustee in connection with the administration of a bankrupt estate, the right of respondent to a set off is governed by the Bankruptcy Act, and the decisions of this Court on the subject are controlling:

Whaley v. *King,* 141 Tenn. 1, 6, 206 S. W. 31.

Section 68 of the Bankruptcy Act provides that in case of "mutual debts or mutual credits" between the estate of the bankrupt and a creditor the account shall be stated, and one debt shall be set off one against the other, etc.

The action of petitioner in the instant case, while in form *ex contractu,* is founded in fact upon a tort:

Chaffee v. *United States,* 18 Wall. 516, 21 L. Ed. 908.

This Court holds that a claim of this character does not become a "debt" when reduced to judgment (*Chase* v. *Curtis* (1885), 113 U. S. 452, 28 L. Ed. 1038; *Wetmore* v. *Markoe,* 196 U. S. 68, 49 L. Ed. 390); that such claims and liabilities as are here presented are held in inconsistent relations, are not of the same quality, are not claimed one from the other in the same right and that set off in such case is not permissible under Section 68 (a) of the Bankruptcy Act.

Libbey v. *Hopkins,* 104 U. S. 303, 26 L. Ed. 769;
Daykin v. *Bailey,* 290 U. S. 143, 78 L. Ed. 229.

In the following cases this Court held that in an action by a national bank the borrower cannot apply the amount of usurious or illegal payments of interest as a credit upon or set off against the amount owing by him to the bank:

Barnet v. *Muncie National Bank* (1878), 98 U. S. 555, 25 L. Ed. 212;
Driesbach v. *Second National Bank* (1881), 104 U. S. 52, 26 L. Ed. 658;
Haseltine v. *Central National Bank* (1901), 183 U. S. 132, 46 L. Ed. 118.

To grant respondent the right of set off under the facts here presented would be subversive of Section 57 (g) of the bankruptcy act (11 U. S. C. A., Section 93-g), the intent of which is that fraudulent or illegal transferees shall surrender their transfers in full before their claim to a dividend shall be allowed. If the set off be allowed to defeat petitioner's recovery respondent will, to this extent, collect its claim in full, and the illegal transaction will thus be perpetuated.

Page v. *Rogers,* 211 U. S. 575, 53 L. Ed. 332;
Lytle v. *Andrews* (8 C. C. A., 1929), 34 F. (2d) 352.

The three State courts concur in holding that the right of set off did not exist until decree was rendered in favor of petitioner; and under every applicable decision of this Court there can be no right of set off unless the same existed at the time of the adjudication in bankruptcy: *Daykin* v. *Bailey,* 290 U. S. 143, 78 L. Ed. 229, and the cases therein cited.

The right to set off is controlled by the Bankruptcy Act, the provisions of which are paramount to any common or statutory law of the several States. *Stellwagen* v. *Clum,* 245 U. S. 605, 62 L. Ed. 507. A Federal question is presented and the decision of the Supreme Court of Tennessee is therefore reviewable by this Court upon petition for certiorari:

Williams v. *Heard,* 140 U. S. 529, 35 L. Ed. 550;
Rector v. *City Dep. Bank,* 200 U. S. 405, 50 L. Ed. 527.

(3) *Right of Respondent to Set Off under State Statute, or under General Principles of Equity Jurisprudence.*

The State Supreme Court was of opinion (R. 82) that set off in such cases as the present is expressly authorized by Section 8769 of the Code of Tennessee (1932), with respect to "Set off of *mutual debts* of a different nature," and also under general principles of equity jurisprudence. This holding is contrary to repeated decisions of this Court to the effect that where a cause of action arises exclusively under the laws of the United States the right to recover cannot be influenced by local law or usage as to set off or counterclaim:

United States v. *Robeson,* 34 U. S. 319, 9 L. Ed. 142;
Barnet v. *Muncie National Bank,* 98 U. S. 555, 25 L. Ed. 212;
Haseltine v. *Central National Bank,* 183 U. S. 132, 45 L. Ed. 118.

To award petitioner a decree for the penalty prescribed by the Federal statute, and in the same action allow respondent a set off under a State statute is to administer the rights of the parties upon distinct and wholly inconsistent theories. This is not permissible.

There was here an unconstitutional exercise of authority under a valid State statute, and the question is one, therefore, for review by this Court upon petition for certiorari:

Zucht v. *King,* 260 U. S. 174, 177, 67 L. Ed. 194, 198.

Petitioner seeks to enforce a thoroughly established legal right, and the maxim *equitas sequitur legem* applies.

Hedges v. *Dixon County,* 150 U. S. 182, 37 L. Ed. 1044.

The Federal right set up in the State court was denied in substance and effect by interposing a non-Federal ground of decision having no fair support. There is thus presented a question upon which petitioner is entitled to invoke the judgment of this Court:

Ancient Egyptian, etc., Order v. *Michaux,* 279 U. S. 737, 73 L. Ed. 931;

Norris v. *State of Alabama,* 294 U. S. 587, 79 L. Ed. 1974.

VI.

ARGUMENT.

(1) Conflict with Applicable Decisions of This Court.

This is an action by petitioner as trustee in bankruptcy to recover the penalty prescribed by the National Banking Act, Sections 5197, 5198, U. S. Revised Statutes (12 U. S. C. A., Sections 85, 86).

The applicable portion of Section 5197, U. S. Revised Statutes (12 U. S. C. A., Section 85), reads as follows:

> "Any association may take, receive, reserve, and charge on any loan or discount made, or upon any

notes, bills of exchange, or other evidences of debt, interest at the rate allowed by the laws of the State, Territory, or District where the bank is located, or at a rate of 1 per centum in excess of the discount rate on ninety-day commercial paper in effect at the Federal reserve bank in the Federal reserve district where the bank is located, whichever may be the greater, *and no more,*" etc.

The penalty prescribed for a violation of the foregoing section is set forth in Section 5198, U. S. Revised Statutes (12 U. S. C. A., Section 86), which reads as follows:

> "The taking, receiving, reserving, or charging a rate of interest greater than is allowed by the preceding section, when knowingly done, shall be deemed a forfeiture of the entire interest which the note, bill, or other evidence of debt carries with it, or which has been agreed to be paid thereon. In case the greater rate of interest has been paid, the person by whom it has been paid, or his legal representatives, may recover back, in an action in the nature of an action of debt, twice the amount of the interest thus paid from the association taking or receiving the same: *Provided,* that such action is commenced within two years from the time the usurious transaction occurred."

This Court has uniformly held that the remedy prescribed by the statute for the recovery from a national bank for usurious interest actually paid is exclusive of all others. Thus, in *Barnet* v. *Muncie National Bank* (1878), 98 U. S. 555, 25 L. Ed. 212, the Court held that as the illegal interest had been *paid,* it could not be applied by way of set off or payment in an action on the obligation. After pointing out that the statutes of the States of Ohio and Indiana could not affect the case, and in holding that the specific remedy provided by the statute alone applied, it was said:

> "The remedy given by the statute for the wrong is a penal suit. To that the party aggrieved or his legal

representative must resort. He can have redress in no other mode or form of procedure. The statute which gives the right prescribed the redress, and both provisions are alike obligatory upon the parties.

"While the plaintiff in such cases, upon making out the facts, has a clear right to recover, the defendant has a right to insist that the prosecution shall be by a suit brought specially and exclusively for that purpose, where the sole issue is the guilt or innocence of the accused, without the presence of any extraneous facts which might confuse the case and mislead the jury to the prejudice of either party."

This case is cited and the rule applied in the following later cases:

Driesbach v. *Second National Bank* (1881), 104 U. S. 52, 26 L. Ed. 658;

Haseltine v. *Central National Bank* (1901), 183 U. S. 132, 45 L. Ed. 118.

The rule laid down in *Barnet* v. *National Bank, supra,* has never been departed from.

While this Court has never passed upon the precise question here presented, other courts have held, in cases where the right of set off was claimed by the bank against the borrower, that the principle announced by this Court in the foregoing cases applies with full force, and that the right of set off, denied to the borrower as aforesaid, cannot be extended to the violator of the statute when sued by the party for whose protection it was enacted. Thus, in *Morehouse* v. *McRae,* 30 Hun. 628 (reversed on the ground of accord and satisfaction, 98 N. Y., 552), in passing upon the question of whether the bank could avail itself of the balance due from the borrower as a set off against the claim for the statutory penalty, the Court said (page 630):

"In the case of *National Bank of Auburn* v. *Lewis* (*supra*) it was held, following *Barnet* v. *National Bank*

(98 U. S., 555), that a cause of action for the penalties in question could not be offset in an action for the amount due on the notes; and it would seem, on principle, that the rule must work both ways. Indeed, the reasoning of the two decisions last cited is applicable to the one case as to the other. The action given by the statute is in the strictest sense a penal action. The penalty is incurred the moment the illegal interest is exacted and received; and in the case of *Barnet v. Bank*, the Court said that the penalty can be recovered only in an action 'where the sole issue is the guilt or innocence of the accused, without the presence of any extraneous facts which might confuse the case,' etc. This is directly to the effect that in an action for the penalty no other question can be litigated than the question whether the illegal interest was received; and such, I suppose, is the rule in all penal actions."

The same rule was followed in *Lebanan National Bank* v. *Karmany*, 98 Pa. 65.

In *Meredith* v. *National Bank*, 127 Tenn. 90, the Supreme Court of Tennessee declined to permit the application of payments made, whether intended as interest payments or not, to that portion of the obligation of the borrower which remained unpaid. The Court says, page 93, that such a result has been reached by some courts in construing usury statutes of the different States—

> "but the act of congress with reference to national banks is strictly a penalty statute and no Court has held that payment of the debtor's obligation in full is a condition precedent to the bringing of a suit for recovery thereunder."

The Court accordingly reversed the decree of the Chancellor sustaining the demurrer and dismissing the bill.

The borrower, for whose benefit the act was passed, is not allowed, in an action by the bank, to apply the illegal or usurious payments as a credit upon the balance owing by

him. It would seem therefore a discrimination against the borrower and a denial of the equal protection of the laws to grant this same right to the bank when the borrower brings a suit "specially and exclusively for the purpose" of recovering the penalty. It is believed that the decree of the State Supreme Court accomplishing this result constitutes a violation of the Fourteenth Amendment to the Constitution of the United States, under the rule laid down by this Court in *Tinsley* v. *Anderson,* 171 U. S. 101, 43 L. Ed. 91, and *Scott* v. *McNeal,* 154 U. S. 34, 38 L. Ed. 896.

Petitioner brings this suit under the provisions of the National Banking Act (12 U. S. C. A., 85, 86), and in substance and effect the decision of the Supreme Court of Tennessee was adverse to the right and the remedy prescribed by such statute. It is believed that this Court therefore has jurisdiction of the case, under the express terms of Section 237 (b) of the Judicial Code as amended (28 U. S. C. A., Section 344 (b).

Talbot v. *Sioux City National Bank,* 185 U. S. 182, 46 L. Ed. 862;

U. S. v. *Bank of New York,* 296 U. S. 463.

(2) Right of Respondent to Set Off Under Section 68 (a) of Bankruptcy Act.

If the matter of set off is entitled to any consideration whatever in a suit to recover the penalty provided by the National Banking Act, in the present instance this right must be controlled by the express provisions of Section 68 (a) of the Bankruptcy Act.

Stellwagen v. *Clum,* 245 U. S. 605, 62 L. Ed. 507;

Whaley v. *King,* 141 Tenn. 1-6, 206 S. W. 31.

Section 1 (11), of the Bankruptcy Act (11 U. S. C. A., Section 1 (11)), provides that the word "debt" shall include any debt, demand or claim provable in bankruptcy.

Section 68 of the act (11 U. S. C. A., Section 108) provides:

> "(a) In all cases of mutual debts or mutual credits between the estate of a bankrupt and a creditor the account shall be stated and one debt shall be set off against the other, and the balance only shall be allowed or paid."

Also that:

> "(b) A set off or counterclaim shall not be allowed in favor of any debtor of the bankrupt which is not provable against the estate."

While the form of the present action is *ex contractu* it is in fact a *tort* action, as directly held by this Court in *Chaffee* v. *U. S.*, 18 Wall. 516, 21 L. Ed. 908; and the fact that a decree had been rendered does not change the nature of the liability of respondent, or the relation between the parties. The claim for the penalty does not become a "debt" after the rendition of judgment.

Chase v. *Curtis* (1885), 113 U. S. 452, 28 L. Ed. 1038;
Wetmore v. *Markoe*, 196 U. S. 68, 49 L. Ed. 390.

Prior to the filing of the petition in bankruptcy the Hamilton National Bank was a creditor of the Lookout Planing Mills and the latter was its debtor because of borrowed money. The bank owed the Lookout Planing Mills nothing. There was no mutuality of debts and credits between the Lookout Planing Mills and the bank when the petition was filed, which is the time when the right of set off must be measured. *Daykin* v. *Bailey*, 290 U. S. 143, 78 L. Ed. 229, and cases there cited. At that time by virtue of law there came to the trustee in bankruptcy, the petitioner here, the right to recover the penalty sued for. This right was exercised and bore fruit. It was translated from a right to recover for the benefit of creditors into actual ownership of

the decree against the bank. The obligation of the bank to pay the penalty, before and after judgment, became the trustee's property. There was never any mutuality of debts and credits between the bank and the Lookout Planing Mills, or the bank and the trustee. It is the same as if the trustee after his appointment had deposited funds of the estate with the bank. There would then have been no right of set off; mutuality of debt and credit at the time of the filing of the petition, or at any other time, would have been lacking.

McDaniel National Bank v. *Bridwell* (8 C. C. A., Nov., 1934), 74 F. (2d) 331.

Aside from other considerations, this Court has jurisdiction of the case upon petition for certiorari because of the misconstruction and misapplication of the Bankruptcy Act to the facts here presented.

Williams v. *Heard,* 140 U. S. 529, 35 L. Ed. 550;
Rector v. *City Dep. Bank,* 200 U. S. 405, 50 L. Ed. 527.

(3) Right of Respondent to Set Off Under State Statute and General Principles of Equity Jurisprudence.

The caption of the State statute (Tenn. Code 1932, Section 8769) reads:

"Set-off of *mutual debts* of a different nature."

The act itself provides:

> "*Mutual debts* * * * between the parties to a suit * * * may be set off against each other. * * * And if either *debt* arose by reason of a penalty, the sum intended to be set off shall be pleaded in bar," etc. (Italics ours.)

The State statute thus, by its very terms, applies only to a set off of *mutual debts,* and not to other causes of action. There is no mutuality of debt between petitioner

and respondent, as petitioner does not owe the bank anything. There has never existed the relation of mutual debtor and creditor.

The provision of the Federal statute for the "recovery back, in an action in the nature of an action of debt, twice the amount of interest thus paid" would be nugatory if the State Supreme Court could be allowed to enter a decree in favor of petitioner under the Act of Congress, and then direct that this decree be applied as a set off against or payment upon the amount owing to the bank by the bankrupt. To permit such practice would lead to a varying measure of responsibility in the several States in which the question of liability might arise, depending upon the conceptions of the State Courts of last resort as to the meaning of the Act of Congress, and some counter right under some common or statute law of the State. The error in the decision below becomes at once apparent when its correctness is tested by the rule that the statute is applicable and furnishes the exclusive test of liability of respondent, and the corresponding right of petitioner.

Yates v. *Jones National Bank*, 206 U. S. 179, 51 L. Ed. 1002, 1014.

In *Barnet* v. *Muncie National Bank* (1879), 98 U. S. 533, 25 L. Ed. 212, suit was brought by the bank upon a bill of exchange, and the payment of usurious interest was set up as an offset or defense. This Court said:

> "The statutes of Ohio and Indiana upon the subject of usury may be laid out of view. They cannot affect the case."

In *Haseltine* v. *Central National Bank* (1901), 183 U. S. 132, 46 L. Ed. 118, this Court holds that usurious interest paid in cash cannot be set off in an action upon the note, and that the remedy provided by U. S. Revised Statutes,

Section 5198, for the recovery of twice the amount thereof in an action in the nature of an action of debt is exclusive.

In *Schuyler National Bank* v. *Gadsden*, 191 U. S. 451, 48 L. Ed. 258, Mr. Justice White delivering the opinion of the Court, the question for decision was, Did the Supreme Court of Nebraska rightly decide that the controversy concerning usurious interest paid was to be governed by the statutes of Nebraska on that subject and not by the laws of the United States on the same subject, as expressed in Section 5198 of the Revised Statutes? In holding that if the rights of the parties were to be determined by the laws of the United States the ruling below was erroneous, the Court said:

> "This results from the prior adjudications of this Court, holding that where usurious interest has been paid to a national bank, the remedy afforded by 5198 of the Revised Statutes (U. S. Comp. Stat. 1901, p. 3493), is exclusive, and is confined to an independent action to recover such usurious payments. *Haseltine* v. *Central Nat. Bank*, 183 U. S. 132, 46 L. Ed. 118, 22 Sup. Ct. Rep. 50, and cases cited."

The Court concluded that the reasoning by which the judgment of the Supreme Court of Nebraska was controlled was erroneous in so far as it held that the remedy as to usurious interest was governed exclusively by the State law. On this point the Court said:

> "As the usurious interest for which a remedy was afforded has been paid to the bank in dealings by the bank with its debtor, and as the necessary effect of the judgment below was to reduce the debt due to the bank by allowing the imputation of the sum of the usurious interest, we are of opinion that the controversy was governed by the laws of the United States, and not by the law of the State of Nebraska."

The Court also pointed out that the fact that the bank had accepted real estate security for the payment of the

indebtedness, in violation of the provisions of the Banking Act, did not operate in any way to modify the conclusions above expressed, and the Court accordingly held that the Supreme Court of Nebraska had erroneously determined the rights of the parties by the rule of the State law when it should have applied the law of the United States.

In *Farmers' & M. National Bank* v. *Dearing,* 91 U. S. 29, 23 L. Ed. 196, it was held that the law of New York forfeiting the entire debt for usury was superseded by the national banking law, and that the Federal statute only was to be regarded in determining the penalty for the usury.

The State court said petitioner had invoked the jurisdiction of a court of equity and that for this reason he would "be required to do equity by having his claim credited on the larger one owing to the defendant" (Opinion, R. 82). The State Supreme Court overlooked the rule that courts of equity are bound by positive provisions of a statute equally with courts of law, and they have no right to deny a well-established legal right upon considerations of general equitable principles. This Court states the applicable rule in *Hedges* v. *Dixon County,* 150 U. S. 182, 37 L. Ed. 1044, to-wit:

> "The established rule, although not of universal application, is that equity follows the law, or, as stated in *Magniac* v. *Thomson,* 56 U. S., 15 How. 299 (14: 703), 'that wherever the rights or the situation of parties are clearly defined and established by law, equity has no power to change or unsettle those rights or that situation, but in all such instances the maxim *equitas sequitur legem* is strictly applicable.' "

It was further said in this case:

> "Courts of equity can no more disregard statutory and constitutional requirements and provisions than Courts of law. They are bound by positive provisions of a statute equally with courts of law."

Petitioner does not claim that the State statute with respect to set off is unconstitutional, or that principles of general equitable jurisprudence may not be considered in proper cases. In the instant case it is believed there is an unconstitutional grant of the right of set off to respondent under a valid statute and under equitable considerations which have no proper application, and for this reason there is presented a question for review and correction by this Court upon petition for certiorari.

Zucht v. *King*, 260 U. S. 174-179, 67 L. Ed. 194, 199.

Conclusion.

It is, therefore, respectfully submitted that this case is one calling for the issuance of a writ of certiorari and the exercise by this Court of its supervisory powers, in order that the decree of the Supreme Court of the State of Tennessee, entered May 24, 1937, modifying and affirming the decree of the Court of Appeals of the State in the case styled on its docket *C. C. McCollum, trustee,* v. *Hamilton National Bank of Chattanooga,* may be modified and reversed by this Honorable Court, in so far as it provides that the amount of the indebtedness of the bankrupt to respondent shall be applied as a set off against or payment of the decree in favor of petitioner.

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